

## Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 SSO-00 NSCE-00 USIE-00 INRE-00 AID-05

CEA-01 CIAE-00 COME-00 EB-07 EA-06 FRB-03 INR-07

IO-10 NEA-09 NSAE-00 OPIC-03 SP-02 TRSE-00 CIEP-01

LAB-04 SIL-01 OMB-01 PA-01 PRS-01 FEA-01 ERDA-05

DODE-00 FPC-01 H-02 INT-05 L-02 NSC-05 PM-03 SAM-01

OES-03 SS-15 STR-01 /119 W  
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O 141924Z MAR 75

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TO SECSTATE WASH DC IMMEDIATE 6004

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PASS TREASURY FOR PARSKY AND WIDMAN,  
EB/IFD/OMA FOR RYAN

E. O. 11652: N/A

TAGS: EFIN, OECD, EINV, ENRG

SUBJECT: PAPERS FOR IEA AD HOC GROUP ON FINANCIAL AND  
INVESTMENT ISSUES (FII): PART II(A) (PAPER  
ON BALANCE OF PAYMENTS ADJUSTMENT AND  
RECYCLING)

REF: (A) OECD PARIS 5996; (B) OECD PARIS 5872;  
(C) STATE 55605

1. MISSION HAS BEGUN RECEIVING FROM SECRETARIAT  
PRELIMINARY DRAFTS OF "COMMENT OR POSITION" PAPERS, IN  
ACCORDANCE WITH ASSIGNMENT OF RESPONSIBILITIES MADE AT  
LAST MEETING OF IEA GOVERNING BOARD AND OF AD HOC GROUP  
ON FINANCIAL AND INVESTMENT ISSUES ON MARCH 6 (REFTEL A).  
INDIVIDUAL POSITION PAPERS WILL BE TRANSMITTED BY  
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SEPARATE CABLES

2. THIS CABLE TRANSMITS THE FOLLOWING PAPER ENTITLED  
BALANCE OF PAYMENTS ADJUSTMENT AND RECYCLING, WHICH  
CORRESPONDS TO ITEM II(A) OF THE TABLE CONTAINED IN  
DOCUMENT IEA/SPC(75)7 SECOND REVISION, CITED IN REFTEL  
A.

BEGIN TEXT

II(A) BALANCE OF PAYMENTS ADJUSTMENT AND RECYCLING

1. THE IMMEDIATE BALANCE OF PAYMENTS EFFECT OF THE  
INCREASE IN OIL PRICES WAS TO SWING THE BALANCE FOR  
CONSUMING COUNTRIES AS A GROUP INTO MASSIVE DEFICIT  
WHICH, IT WAS AGREED, HAS LARGELY TO BE ACCEPTED IN THE  
SHORT RUN. IN 1974, THE EXPORT EARNINGS OF OIL  
PRODUCING COUNTRIES INCREASED BY ALMOST \$70 BILLION. AS  
OIL PRODUCING COUNTRIES COULD SPEND ONLY A SMALL PROPOR-  
TION OF THIS INCREASED REVENUE ON IMPORTED GOODS AND  
SERVICES (ABOUT \$15 BILLION), THE OVERALL CURRENT  
BALANCE OF THE CONSUMER COUNTRIES NECESSARILY  
DETERIORATED SUBSTANTIALY. IN 1974, THE OECD CURRENT  
ACCOUNT WORSENEED BY ALMOST \$35 BILLION TO A DEFICIT OF  
SOME \$33 BILLION. THE CURRENT ACCOUNT DEFICIT OF NON-  
OIL LDCS ROSE BY SOME \$12 BILLION (OR ABOUT \$25 BILLION  
IF OFFICIAL AID TRANSFERS ARE NOT TAKEN INTO ACCOUNT)  
TO \$14 BILLION. THE SINO-SOVIET AREA AND RELATIVELY  
DEVELOPED NON-OECD COUNTRIES ALSO HAD DETERIORATIONS  
ON CURRENT ACCOUNT(1).

2. FOR THE OECD COUNTRIES, THE LARGE DETERIORATION ON  
CURRENT ACCOUNT OF THE AREA AS A WHOLE GAVE RISE TO TWO  
IMMEDIATE CONSIDERATIONS. IT WAS CLEAR, FIRST, THAT THE  
USE OF TRADITIONAL BALANCE OF PAYMENTS ADJUSTMENT  
POLICIES (OR TRADE RESTRICTING POLICIES) TO  
IMPROVE INDIVIDUAL OECD POSITIONS COULD ONLY BE AT THE  
EXPENSE OF OTHER OECD COUNTRIES: HENCE THE  
IMPORTANCE OF AVOIDING POLICY RESPONSES LIKELY TO BE  
COUNTER PRODUCTIVE. THE SECOND CONSIDERATION WAS  
WHETHER EACH OECD COUNTRY COULD ATTRACT SUFFICIENT  
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CAPITAL INFLOW (DIRECTLY FROM OPEC COUNTRIES OR  
OTHERWISE) TO FINANCE ITS DEFICIT. IN THE EVENT THERE  
HAVE, SO FAR, BEEN ONLY LIMITED DIFFICULTIES UNDER  
EITHER OF THESE HEADINGS. THE OECD TRADE PLEDGE,  
ADOPTED LAST MAY, HAS HELPED TO PREVENT "BEGGAR-THY-  
NEIGHBOUR" TRADE POLICIES. AND INDIVIDUAL OECD  
DEFICITS HAVE, TO DATE, BEEN FINANCED LARGELY THROUGH  
THE FINANCIAL MARKETS (IN PARTICULAR THE EURO-CURRENCY

MARKET) SUPPLEMENTED BY DIRECT OFFICIAL (OR SEMI-OFFICIAL) BORROWING BY CERTAIN COUNTRIES. IT APPEARS

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THAT NON-OIL DEVELOPING COUNTRIES WERE ABLE TO GO ON IMPORTING IN LINE WITH DEVELOPMENT REQUIREMENTS UNTIL WELL ON INTO 1974 DESPITE THEIR VERY SHARPLY INCREASED OIL IMPORT BILL, CEASING THE RESERVE BUILD-UP WHICH, IN 1973, HAD AMOUNTED TO \$9 BILLION.

(FOOTNOTE 1: THESE CHANGES FROM 1973 TO 1974 WERE NOT COMPLETELY DUE TO OIL; THE OECD BALANCE WITH NON-OIL DEVELOPING COUNTRIES APPEARS TO HAVE IMPROVED BY AT LEAST \$5 BILLION IN 1974.)

3. IN 1974 THE CURRENT ACCOUNT SURPLUS OF THE OPEC COUNTRIES (ALMOST \$60 BILLION ON A PAYMENTS BASIS) WAS MAINLY FINANCED BY INVESTMENT FLOWS TO THE USA

(19 PERCENT)THE UK (11)HE EUROMARKETS (36 PERCENT), CONTINENTAL EUROPE AND JAPAN (7 PERCENT) AND BY FLOWS TO INTERNATIONAL INSTITUTIONS AND LDCS (10 PERCENT).

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4. BY THE LATER MONTHS OF 1974, HOWEVER, THERE WERE SIGNS THAT FINANCING DIFFICULTIES MIGHT INCREASE. SO FAR AS THE LDCS ARE CONCERNED, PRESENT FORECASTS OF LIKELY FINANCIAL RESOURCES SUGGEST THAT THEY WILL BE CONSTRAINED TO CUT THEIR IMPORTS SERIOUSLY IN 1975, WITH POSSIBLE SEVERE EFFECTS ON DEVELOPMENT IN SOME OF THEM. AND IN RESPECT OF OECD COUNTRIES THERE WAS INCREASING DOUBT WHETHER, WITHOUT SPECIAL NEW ARRANGEMENTS, THE RECYCLING OF FUNDS WOULD PROCEED AS RELATIVELY SMOOTHLY AS IN 1974. HENCE THE ARRANGEMENTS BEING MADE TO PROLONG THE SPECIAL IMF OIL FACILITY AND ENLARGE IT BY \$6 BILLION FOR 1975, AND TO CREATE, FOR TWO YEARS, INSIDE OECD, A SUPPORT FUND, AMOUNTING TO SOME \$25 BILLION TO HELP, UNDER CERTAIN CONDITIONS, MEMBER COUNTRIES WITH PARTICULARLY ACUTE FINANCING DIFFICULTIES. THESE TWO SCHEMES, OPERATING ON RATHER DIFFERENT BASES (1), ARE SEEN AS COMPLEMENTARY EFFORTS TO FACILITATE REASONABLE RATES OF ECONOMIC GROWTH AND REDUCE THE DANGER OF UNILATERAL RESORT TO RESTRICTIVE TRADE PRACTICES OR TO ARTIFICIAL STIMULI TO EXPORTS.

(FOOTNOTE 1: THE OIL FACILITY WOULD, PRIMARILY BUT NOT EXCLUSIVELY, BORROW FROM OPEC COUNTRIES UNDER THE COLLECTIVE GUARANTEE OF THE IMF AND MAY MAKE LOANS AT BELOW-MARKET RATES. THE OECD SUPPORT FUND WOULD, ESSENTIALLY, OBTAIN ITS RESOURCES THROUGH OECD COUNTRIES AND LEND TO THEM ON MARKET TERMS.)

5. THE MASSIVE IMPACT OF THE OIL PRICE-RISE ON OECD'S CURRENT ACCOUNT, AND THE IMPORTANT CO-OPERATIVE ACTION BEING TAKEN TO EASE THE FINANCING OF THE RESULTING DEFICIT, MUST NOT BE ALLOWED TO MASK THE FACT THAT, BEFORE THE OPEC DECISIONS, THERE WERE SERIOUS DIFFERENCES BETWEEN THE RELATIVE STRENGTH OF THE PAYMENTS POSITIONS OF INDIVIDUAL OECD COUNTRIES, AND THAT MANY OF THESE DIFFERENCES GREW IN 1974(2). THE NON-OIL POSITION OF GERMANY, FOR EXAMPLE, WAS SUFFICIENTLY STRONG TO PRODUCE A TOTAL CURRENT SURPLUS OF NEARLY \$10 BILLION IN 1974 DESPITE THE ADVERSE EFFECTS OF HIGHER OIL PRICES, WHILE GROWING NON-OIL DEFICITS REINFORCED THE OIL IMPACT AND PRODUCED CURRENT DEFICITS

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OF \$9 BILLION IN THE UNITED KINGDOM AND \$7-1/2 BILLION IN ITALY. THIS CLEARLY SUGGESTS THE NEED FOR SOME IMPORTANT INTRA-OECD ADJUSTMENTS OF CURRENT ACCOUNT POSITIONS -- I.E. FOR TRADITIONAL BALANCE OF PAYMENTS ADJUSTMENT POLICIES IN AT LEAST SOME OECD COUNTRIES. IN THE ABSENCE OF SUCH ADJUSTMENTS, IT MAY BE DIFFICULT FOR ANY ARRANGEMENTS TO HELP FINANCE WHAT MAY BE REGARDED AS TEMPORARILY INELUCTIBLE OIL-INDUCED DEFICITS TO WORK EFFICIENTLY. WHILE IT MAY BE DIFFICULT TO DEFINE A PRECISE SET OF AIMS ON WHICH TO BASE AN "EQUITABLE" DISTRIBUTION OF THE GLOBAL DEFICIT, THE IMBALANCES ARE SO GREAT AT THE MOMENT THAT THE DIRECTION OF NECESSARY MAJOR ADJUSTMENTS IS CLEAR. THE EXTENT TO WHICH THIS ADJUSTMENT TAKES PLACE WILL HAVE AN IMPORTANT BEARING ON THE MEDIUM-TERM FINANCING QUESTION. AT THE TIME OF WRITING, THE PROSPECTS FOR 1975 ARE THAT WEAK DEMAND WILL SEE OECD'S CURRENT ACCOUNT DEFICIT FALL BELOW THE \$30 BILLION, BUT THAT WITHIN THIS TOTAL THE DISTRIBUTION BETWEEN OECD COUNTRIES WILL REMAIN EXTREMELY UNEVEN. (FOOTNOTE 2: SEE "ECONOMIC OUTLOOK" NO. 16; DECEMBER 1974, PP. 60-2 FOR MORE DETAIL ON THIS POINT.)  
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